

## **Was the Middle East’s Economic Decline a Legal or Political Failure? A Review of Timur Kuran’s “*The Long Divergence: How Islamic Law Held Back the Middle East*”**

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“Law, like politics, is a meeting place for ethics and power”

E. H Carr (1946)

### **I. Introduction**

One of the staple questions of economic history and development relates to why Europe was the first to achieve industrialization and stable growth. Much ink has been spelt on identifying sources of divergence between Europe and Asia. In his new and well acclaimed book, *The Long Divergence: How Islamic Law Held Back the Middle East*, famous economist Timur Kuran traces the causes of divergence between Europe and the Muslim Middle East – a region that has been less emphasized in these divergence stories. But Kuran’s focus is opposite: the “fall of Middle East” rather than the rise of Europe. In thinking about divergence, Kuran has fallen back on a refined and modified version of the much trumpeted cultural argument that Islam is inimical to development.

The idea that Islam is inimical to development is not new, dating back to the influential writings of eminent cultural theorists such as Montesquieu (1689–1755), Edmund Burke (1729–97), James Mill (1773–1836), Alexis Tocqueville (1805–59), John Stuart Mill (1805–73), Karl Marx (1818–83) and Max Weber (1864–1920)<sup>2</sup> and Bernard Lewis (1916-). It is asserted that Islamic nations possessed cultural traits, such as fatalism, absence of strong work ethics, which prevented them from making economic progress. This thesis was endorsed by the fact that unlike Christianity, Islam did not go through any reformation. The path of development in the Islamic world was therefore truly seen through the Western lens. This view, however, has been readily dismissed by a spate of recent empirical studies that have failed to find any convincing evidence in favour of this cultural explanation. This thesis has also been readily dismissed by cultural critics including Timur Kuran, in his earlier book *Islam and Mammon* on the simple ground that if there was something intrinsic in Islam that deterred development then how would one account for the rise of Islam and the associated economic prosperity in the pre medieval period? Given the geographic and cultural diversity of the Muslim world and the multiple prisms through which Islam is understood, interpreted and practiced in various parts of the world, it is easy to disprove that Islam could be viewed as a single cause for the underdevelopment of the Muslim world.

In his recent book, *The Long Divergence*, Timur Kuran advances a more refined and

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<sup>2</sup> Michael Curtis, *Orientalism and Islam: European Thinkers on Oriental Despotism in the Middle East and India* (Cambridge: Cambridge University Press, 2009),

nuanced version of his thesis. In Kuran's view it is not Islam *per se* that prevents development, but certain aspects of Islamic law that govern commercial and economic relations that are unfavourable for long run economic development.

### **I.I The argument**

The core arguments of this book are derived from a series of research papers that Kuran wrote in a decade or so. In *The Long Divergence* Kuran weaves a story around these papers. A key contribution of the book is that it offers an alternative, and arguably provocative, explanation for an important historical puzzle: despite having made impressive progress in its earlier history, why did the Islamic Middle East fall behind Western Europe in material progress in post medieval period? The central explanation of Kuran revolves around the role of Islamic law. He identifies four key features of Islamic law that in his view were economically inefficient and prevented the emergence of private commerce.

First, despite being egalitarian the Islamic law of inheritance discouraged the accumulation of wealth by dividing it among family members. The permissibility of polygamy exacerbated this problem as it fragmented the assets of wealthy merchants with multiple wives and children.

Second, Islamic law of contract and commercial partnerships was simple, limiting the continuity of successful enterprises as the death of a partner frequently lead to the dissolution of a partnership. An associated constraint was that Islamic law arguably does not recognise the concept of juristic personality of non-human entities.

Third, the development of large scale enterprises such as joint stock companies with transferable shares and banking companies critically depended on a paper economy that documents and preserves written records. Islamic legal practice, however, did not recognise the evidentiary value of written documents without witnesses. This hampered the rise of paper based economy comprising of paper currency, financial instruments, banks and joint stock companies in the Middle East.

Fourth, Islamic charitable institutions commonly known as waqf, became another hindrance in capital accumulation, as they devoured massive resources that might have been invested in business corporations. Although in the pre-modern era waqf was a key instrument for delivering social services, over time however, it became inflexible and prevented the emergence of alternative organisational forms. According to Kuran this became a particular hindrance in the age of industrialisation.

An associated critique relates to the abhorrence of usury or *riba* (interest in common parlance) in Islam, which arguably deprived the Islamic world of a key stimulus to private commerce: access to credit finance. Although it was cited as an important constraint in some of Kuran's earlier work, this argument appears in a much tempered form in *The Long Divergence*. Clearly interest based finance has been rife in several periods of Islamic history, even under the Ottoman rule. Although laws against interest

were avoided through legal stratagems, such devices imposed their own costs.

The prohibition of apostasy not only discouraged Muslims from criticizing the Islamic legal institutions, it also made it impossible for Muslim merchants to use non-Muslim legal system for conducting their businesses. A combination of the above factors discouraged the accumulation of wealth and the development of impersonal large organizations. It kept both the civil society and merchant classes weak who could not pressurise the political elites for reforms. Therefore, if the Middle Eastern states were and continue to be autocratic, the root cause lies in Islamic law.

## II. Methodology

Timur Kuran's argument about the deleterious effect of Islamic law is essentially a historical argument that is based on deductive reasoning and a set of hypothesized claims. Although some of the claims and underlying mechanisms are supported by selective empirical evidence, principally Ottoman archives, Kuran's central argument is not yet fully substantiated by empirical evidence. Furnishing historical evidence is not easy, especially when the time period involved runs into centuries and potential explanations are numerous. Social scientists interested in explaining long-run development outcomes have attempted to resolve this by searching for natural experiments of history (Nunn 2009, Diamond and Robinson 2010). To the extent that history offers interesting natural experiments, such as slavery or a particular colonial intervention, which could drive a wedge between potential outcomes this offers a convincing approach. A key advantage of using natural experiments to explain divergence in development outcomes is that it can allow us to control for a variety of confounding factors.

Kuran's claims on the developmental impact of Islamic law are neither supported by rigorous empirical evidence nor detailed contextual case studies. Also absent are any latest tools from the arsenal of economic historians (statistical methods, rational choice models, the natural experiments, for example). As such, they remain a series of theoretical claims that are subject to empirical falsification. At best, Kuran's analysis could be construed as establishing an association between aspects of Islamic law and Middle Eastern underdevelopment. It is difficult, however, to accept Kuran's argument as a *causal* claim. The main contribution of *The Long Divergence* is that it offers an interesting and provocative hypothesis that could be subjected to future empirical scrutiny along with other possible explanations. All of this calls for a greater circumspection and a less cavalier approach than what Kuran's analysis entails.

To pursue the methodological issue further, a particular limitation of this analysis is its disregard of other confounding factors and the endogeneity of law to deeper processes, including the nature of political institutions. We discuss these issues separately.

### II. (a) *The possible role of confounding factors*

Even if the primary focus of Kuran's analysis is to explain the sources of Middle Eastern decline, there is relatively limited discussion of the ingredients behind Europe's success. This is both trivial and significant. Discussing the "European miracle" is admittedly a peripheral concern given that considerable intellectual effort has already gone into

explaining the economic rise of Western Europe. Yet, it is a significant omission at another level. It prevents the reader from appreciating that Europe's success had multiple origins. Despite the many disagreements of details, historians agree on at least one thing: the European economic advantage was the culmination point of a number of cumulative processes and mutually reinforcing factors. ["varied and cumulative"] It would therefore be a dangerous over-simplification to reduce the divergence between Europe and other regions to a single cause or one magic bullet (see, for example, Jones ??, Pomeranz 2000, Tilly 1990). To quote famous historian, Eric Jones, "any broad historical evolution has a configuration of causes" (Jones 2003: pg. xviii).

It is clear that the Middle East and Europe differed on several dimensions, not just their legal arrangements. The range of plausible explanations for this divergence in development outcomes is potentially very large. We will focus here only on a handful of factors, simply to draw the reader's attention to other competing explanations that are either ignored by Kuran or not systematically built into his exposition. The first explanation relates to the importance of geographic influences, such as climate, location, resource endowments and the broader geography of trade. Although far from being a singular cause for its success, Europe's environment and physical geography created more favourable conditions for development. Europe's geography was more suitable to regional specialization, long-distance trade, diffusion of technology and political decentralization (Jones 2003). To start with, the scale and intensity of natural disasters was considerably lower in Europe, with the result that Europe suffered less destruction of its capital in the wake of natural disasters than other comparator regions. Europe's geography, especially its low temperatures, low population density and limited agricultural productivity was relatively inauspicious to centralized authoritarian rule. Its location is believed to have provided it relative safety from some of the most rapacious attacks by Eurasian invaders—the Mongols, for example. But, perhaps more importantly, it was the favourable geography of trade that proved most beneficial for exploiting its commercial potential. Europe's long coastlines, the navigability of its rivers and its "dispersed portfolio of resources" played an important part in shaping the region's outward trade orientation. Through its growing trade engagements, Europe was successful in moving beyond the trade of luxury goods to the bulk trade of every day necessities that conferred the region significant advantages in terms of backward and forward linkages with related business activities.

It is in the arena of trade, then, that the contrast between Europe and the Ottoman Empire became more striking over time. For a long time the Middle East profited from its geographic location that placed it at the center of the world's trading routes. Its land-based trade routes were much travelled upon, bringing prosperity to the region and resulting in growing population and sprawling urban centres. But the Middle East gradually lost its trading advantage with the development of alternative and cheap trading routes that bypassed the region "by going south of the African continent". With the fall of the Constantinople and the discovery of the Cape of Good Hope, the land-based trade routes that passed through the Middle East were gradually replaced with sea-based routes. The Atlantic trade, in particular, grew in importance as trade shifted from the Mediterranean to the Atlantic.

This generated a new trade pattern that bypassed the Mediterranean and resulted in a loss of economic advantage for a region that was heavily dependent on trade.<sup>3</sup> Clearly, the shift from land to sea-based trade routes and the rise of the Atlantic trade shifted the balance of economic power against the Middle East. This loss in trading advantage might have militated against the development of private enterprise. Jeffrey Sachs concurs with the important role of this shifting geography of trade in tipping the scales of development against the Middle East. In the modern development discourse, Jeffrey Sachs is credited with establishing the links between geography and development. But, even in Sachs's account, geography is simply one of the many drivers of cross-country income differences besides trade and institutions. Although no one factor exclusively determines development, factors such as the availability of natural resources, global trading routes, ecology, and geography might have played a bigger role in shaping development in the Islamic world than the cultural interpretations offered by Weber and Lewis.

In relation to trade, it is relevant to ask if the shift to sea-based routes following the discovery of the Cape of Good Hope be described as a critical juncture that subsequently drove a wedge between the subsequent development trajectories of the Ottoman Empire and Western Europe. The role of critical junctures, quite apart from this shifting geography of trade, has not been systematically entertained by Kuran. Latest advances in institutional analysis pioneered by eminent political scientists Kathleen Thelen and Paul Pierson highlight the crucial role of temporal dimensions in explaining long-term processes of economic and social change. Recent work in this regard calls for greater attention to the timing and sequencing of events and their "interactions with various processes unfolding at different speeds" (Pierson 2004).

These omissions notwithstanding, trade forms a crucial part of the European success story. But despite its prominence in historical accounts of economic prosperity, it is albeit one of the several factors that collectively shape the development experience (see, for example, David Landes's magisterial work on the Wealth and Poverty of Nations). For instance, throughout human history trade has been intertwined with politics, whether taken as domestic or geopolitics. Clearly, trade requires the facilitation of rulers, but it can also alter the way economic, and therefore political, power is distributed within societies. This is a theme we will touch upon later in this paper, but we begin here by first emphasizing the importance of "external influences" in shaping the "European advantage". Europe's trading success was not achieved through "internal processes" alone, but was aided by a combination of commerce, coercion and colonization. While tracing the evolution of world economy, historians have forcefully argued that a frictionless market mechanism and an efficient organization of economic activity were not the only determinants of prosperity. Historical trade patterns were also crucially influenced, beyond the realm of "consensual trade", by a geo-political context that was

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<sup>3</sup> The Islamic world also faced a significantly more difficult time defending itself, as it lacked the advantage of Western and Eastern regions protected by mountains or bodies of water.

characterized by “plunder, enslavement and conquest”<sup>4</sup>. In their magnum opus, *Power and Plenty*, Robert Findlay and Kevin O’Rourke emphasize the inseparability of trade and empire in the early phases of globalization. The zero-sum character of mercantilist trade in that era led to a struggle between European powers for controlling trade routes and precious resources. Europe’s overseas ventures involving colonization, slave trade, and discovery of the New World afforded it a “privileged access to overseas resources”. Aided by the extra-ordinary scale of these resources, Europe created a system of production that boosted consumer demand at home, created an expanded market for its exports abroad and relaxed the region’s key resource constraints in land and energy (Pomeranz 2000). This is not to suggest that the windfalls from Europe’s overseas conquests were the sole driver of its prosperity. Nor is the objective to “externalize” the causes of European advance to a world system that established a bleak division of labour between the European core and the global periphery, as the works of Immanuel Wallerstein and Andre Gunder Frank might suggest. It is simply to underscore the point that the growth of private commerce and long-distance Atlantic trade were part of a broader process where the “state, colonial ventures and nonmarket extraction”<sup>5</sup> lent a crucial helping hand.<sup>6</sup> While large corporations benefited from special privileges and monopoly rights granted by the state, the forces spearheading this process strengthened both merchants and markets in the long-run.

It is in this backdrop of inter-state competition, overseas expansion, and long-distance trade that European firms invented new organizational forms and financing mechanisms that ultimately manifested in such Western corporate inventions as impersonal and permanently lived organizations, the separation of ownership and control, and the mobilization of long term capital through joint stock companies. Many of these legal and corporate innovations were partly a response to the needs of war-making states and overseas commercial ventures. In fact, until the nineteenth century “family firms dominated most economic activities”<sup>7</sup> in Britain, and:

“It is significant that where eighteenth-century Europeans’ supposedly superior commercial organizations had to compete with merchants from other Old World regions without using force, their record was mediocre. Only in overseas colonization and *armed* trading did Europe’s financial institutions – nurtured by a system of competing, debt-financed states – give it a crucial edge”. Pomeranz (2000, pg. 19)

The rise of East India Company offers a pertinent example. Summarizing Niels Steensgaard’s argument, Pomeranz (2000) elaborates how the fixed costs of East India Company’s military-industrial empire in Asia:

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<sup>4</sup> Findlay and O’Rourke (2007).

<sup>5</sup> Pomeranz (2000): pg. 19.

<sup>6</sup> This was aided in no small measure by other global conjunctures, such as the rising demand for Asian silver.

<sup>7</sup> Pomeranz (2000): pgs. 198-9.

“made it impossible to follow earlier practices in which trading partnerships were completely liquidated after a preset period of time, with all assets distributed back to the partners. Instead it became necessary to treat much of the company’s capital stock as permanent and to retain as much of the profit as possible for circulating capital; this alone made it possible to spread large fixed costs over a sufficiently large volume of trade and adequately compensate investors whose original capital could never be liquidated for return to them. And finally, because not all investors were willing to be patient enough for this sort of enterprise, ownership and control of the firm had to be firmly separated, with a market in shares that allowed dissatisfied owners to exit a permanent arrangement in which they were increasingly denied a voice on policy” (Pomeranz 2000, pg. 193).

All of this underscores the extent to which trade and merchandise were mutually embedded in Europe’s inter-state competition and overseas ventures. Driven by the military imperatives, the European states granted special privileges and monopoly rights to capitalists and entrepreneurs in return for their support in settlement and extraction in new colonies. Back in Europe, many of these companies also profited from the growing market for imports. The development of private enterprise was thus shaped by an external context that strengthened not just the state but also its military and economy. Importantly, the overseas ventures engendered a cooperative framework for merchants—a framework where merchants were favoured rather than feared.

Such alignment between the interests of state elites and merchants was rarely achieved in other regions, including, most notably, the Ottoman Empire especially after the sixteenth century. Ruling elites in the Middle East seldom participated in trade. They rather lived off the revenues generated from landed estates. Under the Ottomans, merchants were tolerated, but neither privileged nor encouraged. And, unlike Western Europe, the Ottoman Empire was rarely faced with circumstances that could have produced mutually compatible incentives for rulers and merchants. This was especially the case after Ottoman age of exploration ended in the late sixteenth century as a result of multiple defeats on various fronts. The state fell upon its internal resources instead of ‘engaging with the dynamic political economy of the world beyond its borders.’ [The Ottoman Age of Exploration, 200]

Going beyond trade and conquests, the coercive competition between European states had some far-reaching effects on the nature of politics and the very process of state formation. As Charles Tilly argues warfare and internal competition, by generating new revenue imperatives set Europe on the path of state formation, strengthening at the same time the state’s fiscal capacity and permitting a healthy transformation from feudalism to fiscalism. Again, the merchants emerged from this as important beneficiaries since, in the absence of an extensive base for land taxation, they became a coveted constituency for meeting the state’s revenue needs. In return for these taxes, merchants won key concessions in the form of greater security of property and relatively free market conditions. These processes solidified not only the cooperative arrangement between rulers and merchants, but also laid the basis for the emergence of property rights and representative government. Perhaps more importantly, Western Europe was able to

realize a virtuous circle that generated two critical ingredients for sustained economic prosperity: constraints on the power of ruling elites and the provision of public goods (Jones 2003). The crucial question, however, is what led to a diffusion of power away from centralized authoritarian rule in key European states. Clearly, limits to the discretionary powers of rulers emerged endogenously due to an array of forces. Even if it is difficult to pin down a single cause, there is broad agreement that greater political decentralization, competition between states, growing dependence of the state on merchants and the rise of trans-Atlantic trade all played a helpful part.

As a centralized and monolithic entity, the Ottoman Empire lacked the economic and political benefits that Europe's decentralized and "competitive state system" offered. Political decentralization and the growing influence of merchants led to a dispersion of power in Europe that checked the "worst arbitrariness" of the state.<sup>8</sup> In contrast, even when the Ottomans were challenged to reform, they did so by centralizing their control and bureaucratizing the state (example: the *Tanzimat* reforms). While Europe "sailed on its commercial revolution", the Ottomans "were confined to the land" (Jones 2003). Merchants did not occupy a prominent position in the Ottoman power structure and commercial revenues paled in significance to those in Europe. The overriding objective of the Ottoman rulers was to prevent the emergence of competitors challenging their rule. And, the merchants potentially fell in this category. Neither the external nor the domestic context was conducive to commerce. In the face of declining participation in international trade and the conservatism of its centralized authoritarian rule, merchants under the Ottoman rule were presented with neither the opportunities nor the incentives for innovation, creativity and entrepreneurship. In the end, these might have served as greater barriers to development than Islamic law.

The voluminous literature that seeks to explain the European advantage is riven with disagreements. But despite these differences in detail and substance, scholars would tend to unite on at least two observations. *First*, the rise of Europe, like any process of socio-economic change, is "politically embedded". It is therefore pertinent to ask whether "Europe's political economy was more conducive to capitalist accumulation"<sup>9</sup> and, if so, why? The question, then, ultimately boils down to politics; it is difficult to disentangle power from prosperity. *Second*, given the "varied and cumulative" processes that went into creating the "European miracle", it is difficult to reduce the region's development experience to a single identifiable cause. There is a need, instead, to give due attention to relevant contexts, interactive relationships and mutually reinforcing processes. The following extracts from two leading economic historians best encapsulate the latter message:

"The Industrial Revolution, in turn, can only be understood as the outcome of a historical process with multiple causes stretching well back into the medieval period, and in which international movements of commodities, warriors, microbes and technologies all played a leading role. Purely domestic accounts of the Rise of

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<sup>8</sup> These benefits did not come, however, at the expense of the economies of scale associated with an Empire.

<sup>9</sup> Pomeranz (2000): pg. 173.



the West, emphasizing western institutions, cultural attributes or endowments are hopelessly inadequate, since they ignore the vast web of inter-relationships between Western Europe and the rest of the world that had been spun over the course of many centuries, and were crucially important for the breakthrough to modern economic growth”. (Findlay and O’Rourke 2007, pgs. 6-7)

Another quote from Jones (2003, pg. 238) underscores the same point:

“In the present state of knowledge we must resist the notion that any simple model will account for the whole developmental process. We cannot model it, say, as a production function which makes modernization, eighteenth century industrialization, or the sustained rise of real incomes, the output of a handful of stylized inputs, while hoping to retain any sense of the historical complexity involved. Too many parameters shift and dissolve; very long-term economic change was much more than the usual conception of an economic process”.

This raises two serious challenges for the Islamic law matters thesis presented by Timur Kuran. First, if Europe’s rise is the result of multiple processes, is it reasonable and defensible to explain the Middle East’s economic decline under the single rubric of Islamic law? Furthermore, does a unidirectional and deterministic relationship between Islamic law and development provide a satisfactory account? Second, how important is the political economy of development in the Middle East, and can law be divorced from politics? The next section takes up the latter question: the possible endogeneity of law to politics.

## II. (b) *Law and politics in the Middle East*

Any legal explanation for development is subject to the criticism that law is ultimately endogenous to politics. It can, at best, serve as a proximate rather than a deep determinant of development. This is easy to understand. Laws and regulations emanate from the wider political process; even their enforcement hinges on the will of political incumbents. But, the question in the context of Timur Kuran’s arguments is whether Islamic law, given its sacred origins and its resistance to change, is impervious to this reasoning. In this section, we argue that even if some parts of Islamic law lack political origins, the way these laws are developed, interpreted and applied can be heavily influenced by the material domain. Historically, Islamic law has not been immune from political influences. And, in this, it is not any more exceptional than secular laws or laws derived from other religious traditions.

The idea that aspects of Islamic law are inimical to development has direct parallels to the “Law Matters Thesis” advanced in the literature on financial development in the 1990s. In thinking about why some countries have developed more able financial systems, some scholars have tended to emphasize the role of a country’s legal origin rooted in its colonial past (La Porta et al. 1998). The key argument here is that some legal traditions, such as the British Common Law, have more favourable consequences for development. It is argued that the common law tradition ensures a better protection of minority shareholders and private property, and responds more flexibly to changing

circumstances (La Porta et al. 1998, 1999, 2008). As a result, countries that inherited a British Common Law tradition are more likely to have developed financial institutions compared to, say, countries with French Civil Law tradition. Of late, the legal origins view has been contested, both theoretically and empirically, by scholars who argue for the primacy of political institutions. In this view, a political system where power is unchecked and concentrated amongst a narrow group tends to limit financial access. There is an inherent conflict of interest between the government's need to raise financing from financial markets and its role as an enforcer of legal contracts. In weak polities this could lead to an opportunistic behavior of governments that compromises long-term development of financial markets (Haber, North and Weingast 2008). With fewer limits on executive discretion, governments are more likely to use the financial system to create rents for their constituents. This can often result in concentrated banking systems that restrict entry in the banking sector and limit competition.<sup>10</sup> There is a strong suggestion here that politics, rather than a country's legal origin, offers the main reason for why some countries are unable to develop open and broad based financial systems. Neither historical nor contemporary evidence supports the legal origins view (Haber, North and Weingast 2008, Mark Roe, Zingales, Guiso).<sup>11</sup>

The view that Islamic law served as the main irritant to economic development in the Middle East echoes some of these debates. Specifically, Kuran's argument is the cultural variant of the growingly discredited "Law Matters" thesis. The crucial question, in light of the discussion above, is whether it is possible to decouple law from politics, even when the sources of law are sacred and less amenable to change over time. In answering this question, we need to understand the interplay between Islamic law and political power, especially during the Ottoman period. Despite its sacred origin – based as it was on Quran and Hadith - Islamic law has to be viewed in relation to wider social and political processes. It is widely recognized that the material context, whether political or economic, shapes forms of religious expression. And, as the ensuing discussion will show, even legal institutions are not exempt from such influences. Their autonomy from the secular domain is only fictional, not real.

In order to explore the institutional underpinning of religious law it is important to throw more light on the role and position of the key actors: Ulama, the religious leaders. Although Islam has resisted the need to create a "church". As a diverse group, the position of Ulama has changed through history – a dynamic, differentiated space. Not a unitary force with the authority to enforce divine law. But over time – and especially under the Ottomans – they have depended on royal patronage for their growth and

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<sup>10</sup> A classic example cited in this regard is the evolution of financial markets in the United States and Mexico. Scholars have traced the origins of differential development of financial markets in United States and Mexico to differences in the underlying political structure. Specifically, the decentralized and competitive political system in the US made restrictions on banking competition unviable. By contrast, the centralized political control in Mexico resulted in a more concentrated banking system (Haber 2008).

<sup>11</sup> MJ Roe, 'Political Determinants of Corporate Governance: Political Context, Corporate Impact' (2003) Harvard Law School John M. Olin Center for Law, Economics and Business Discussion Paper Series. Paper 451 ; L Guiso, P Sapienza and L Zingales, 'Does Culture Affect Economic Outcomes?' (2006) 20 The Journal of Economic Perspectives 23; RG Rajan and L Zingales, 'The Great Reversals: The Politics of Financial Development in the Twentieth Century' (2003) 69 Journal of Financial Economics 5.

survival. [They are appointed by the executive authority, required by rulers to legitimate their rule by providing a religious sanction. Although, originally, there was no papacy in Islam, the entrenched monarchic rule created a somewhat similar situation where the secular and sacred domains were practically separated. *De jure* law was based on the law of the king, but *de facto* in practical matters the law of the king (*kanun*) reigned supreme. Thus, practically there was a neat division of labour between the secular and sacred domains.. The Ottoman rule saw a greater bureaucratization of the religious authorities, with organized hierarchical structures with Sheikh ul Islam at the top. The *qadi* occupied a “central position” in the ottoman provincial administration. [competition for top positions in the hierarchy, with ulama jockeying for positions and privilege] [formed part of the Ottoman nobility and aristocratic classes through whom the governors ruled (Hourani ???)]. Their relations with rulers were more conciliatory than adversarial, and were very much embedded in the political system. [top ulama had ties with princes]. As Zubeida (2011) notes: “senior scholars, as muftis, were quite inventive in formulating legal justifications for whatever their patron rulers wished to institute”.<sup>12</sup> And, “as figures of power and influence, they acted like other politicians, participating in patronage, control of resources and factional struggles, but with the advantage of being able to invoke religious sanction” (pg. 15).

In short, religious authorities under the Ottomans derived significant economic and political privileges. Religious families with a long standing honourable ancestry competed for offices, titles, and, even, tax farms. The office of the qadi dispensed several functions, some of which included revenue generation and other “lucrative functions”. In this respect, it is important to note that the sacred Islamic inheritance law that lies at the heart of Kuran’s analysis did not apply on land. The state was regarded as the owner of all land while peasants were the tenants obliged to pay rents in the form of taxes. Islamic law developed independent of state by personal endeavours of jurists in classic era between the 8<sup>th</sup> and 12<sup>th</sup> centuries. The jurists by their independent legal opinions used to serve a check on the powers of rulers and their opinions were sought in order to confer legitimacy upon the ruling regime. Thus the ruler was never above the law as he was dependent upon jurists not only for legitimacy but also for the validity of his conduct. However, the Ottomans incorporated the legal community into the state system and it was the sultan who used to appoint the Sheikh ul Islam, chief kadi and other key position holders from amongst the legal community. So strong was the alliance of interests between the ruling and legal classes that the constitutional law was never developed in the Ottoman Empire and the issue of putting legal constraints on the coercive powers of the state was never seriously considered.<sup>13</sup>

Awqafs (endowments) offer one crucial way through which religion was materialized. These Islamic charities had religious sanction and were immune to arbitrary expropriation by the state. But, over time, these got degenerated into elaborate systems of rent seeking that can be best understood as the politics of property rights. Agricultural and urban real estate offered stable income streams. Ulama often acted as their

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<sup>12</sup> Zubeida (2011): pg.15

<sup>13</sup> M Cosgel, T Miceli and R Ahmed, 'Law, State Power, and Taxation in Islamic History' (2009) 71 Journal of Economic Behavior & Organization 704, 716.

administrators or overseers. Some endowments were set up by officials and notables out of state owned properties; others by private individuals. A controversial religious order also sanctioned cash waqf that used lending to generate interest income. Examples could be found of even interest based contracts enforced by Shariah courts. Legal justifications existed for some of these practices. So, there were cases where law could be moulded to suit the ruler's needs or the demands of the market. There was also a growing state interference in awqaf. To assume that Islamic law stood as a time invariant body of law that was autonomous from material influences is to ignore the historical complexity of Muslim societies. Thus, any view that that ascribes a greater agency to Islamic law needs to build into the exposition the role of politics.

As mentioned before, groups with the capacity to initiate "political action" were viewed with utmost suspicion. The ruling Ottoman bureaucratic elites jealously guarded the existing socio-political order and tried to thwart any political or economic power that may pose a threat. Thus confiscation of property was a dominant state policy against the wealthy private producers and traders. The wealth accumulated through official privileges could not be bequeathed or divided under Islamic law of inheritance and the state was the heir of the officials exercising an employment under government.<sup>14</sup> However, the state had its limitations in exercising its policy of confiscation as it could ill afford outright elimination of wealthy classes of the society who were instrumental in providing vital services such as merchants and money changers who also provided finance to the state at the time of financial distress. Therefore, where confiscation was unsuitable, the government forced the massive capital holders to take the risky business of supplying meat at fixed prices for Istanbul and the army.<sup>15</sup>

### III. In search of a broader theoretical frame

Even in the absence of detailed evidence, has Prof. Kuran entertained other theoretical possibilities? It remains essentially an institutionalist claim. A possible strength of Kuran's thesis is that it is essentially rooted in the role of institutions, which has long been ignored by economic historians of the Middle East. His focus on waqf as an instrument for the provision of public services and its limitations offers one example. Previously, economists had superficially looked at differences in economic strengths between the two regions.

How law can shape incentives and constrain choices of private agents? A good way of approaching this is to deploy the tools of new institutional economics. Where does Kuran's analysis fit into the various strands of new institutional economics? Given the greater focus on law as the primary explanation, one would ask if law is simply one element of the broader institutional matrix and whether it is justifiable to discount the broader institutional matrix which can determine how laws are interpreted and enforced. An issue of central importance in NIE is to analyze and highlight the institutional structure that allows societies to move from personalized exchange to impersonalized

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<sup>14</sup> T Thornton, *The Present State of Turkey: Or a Description of the Political, Civil, and Religious Constitution, Government, and Laws, of the Ottoman Empire.* (Joseph Mawman 1807) 236-37.

<sup>15</sup> H Inalcik, 'Capital Formation in the Ottoman Empire' (1969) 29 *The Journal of Economic History* 97,139.

exchange. It is clear that societies where economic and political exchange is organized through impersonal exchange can be more readily characterized as developed.

Some of the central issues explored by Kuran are therefore related to a fundamental question in institutional economics: How do societies make a transition from a world of personalized exchange to one of impersonalized exchange? The core function of institutions is to aid that transition and to allow societies to reap the benefits of economic specialization. In primitive societies there is a greater dependence on mutual trust and sanctions and reputation figures more prominently. Cooperative arrangements are more easily enforceable in such situations. As economic exchange becomes more complex, societies need third party enforcement and formal rules to govern transactions. Evolutionary Institutionalism identifies institutions with equilibrium attributes of interacting individuals. It implies that institutional dynamics are a function of evolutionary forces embedded in extreme assumptions on the human nature (Greif). It is by employing this expansive conception that Greif arrives at his central thesis for this research: the effective institutional arrangements of medieval Europe and the Middle East that limited transaction costs and facilitated more efficient economic exchange were based on “intentional and coordinated efforts by many individuals – who were often economic as well as political agents with coercive capabilities” (Greif 389).

Greif’s comparative historical institutional analysis emphasizes a context specific approach to the study of institutions. Kuran is providing the much needed Islamic context, but ignores the other important contexts. At one level Kuran’s book does precisely that; it presents the religious context for the emergence and persistence of Islamic laws governing commerce. But it ignores the other context, which is the wider political and social context. Furthermore, we have a less satisfactory explanation for how societies make a transition from personalised to impersonalised exchange. That still remains the central research question of NIE. Indeed North’s and co-authors have set out an impressive array of arguments around the two social orders in their latest volume

### ***Violence and Social Orders.***

The story of institutional persistence, where there is a clear demarcation between the de jure and de facto distribution of power, stipulates that law and practice can operate in different directions. A key explanation for why inefficient institutions persist is located in the interaction between de jure and de facto power. Kuran gives a lot more importance to de jure factors; what is missing from the analysis, however, is the link between the de jure and de facto power. This has a key implication for Kuran’s work. It is important to set out the de facto distribution of economic and political power in Ottoman Empire. As has been mentioned before, merchants did not occupy a prominent and influential position in the overall power structure.

### ***Trade and politics***

Recent scholarship in institutional economics has emphasized the primacy of long-distance trade in determining political evolution. The mutually reinforcing character of

trade and institutional change is the highlight of a growing body of scholarship. The economic rise of Western Europe has been offered as a case in point in this respect. European divergence of Western Europe and other regions has been a subject of much intellectual enquiry. Daron Acemoglu and James Robinson, whose perspectives on political economy have transformed the discipline in recent years, attribute the rise of Europe to the growth of transatlantic trade since 1500. But the transformative impact of Atlantic trade is conditioned by the initial institutional arrangements of the state. The Acemoglu and Robinson story weaves together two key elements: constraints on the power of the monarchy and the rise of the bourgeois trading class. Where monarchies faced fewer constraints, trade strengthened their political and economic power and they used it to restrict property rights. By contrast places such as Britain and Netherlands where monarchy faced greater initial constraints and which had good coastal access, trade strengthened the power of the merchant groups, leading to the emergence of a trading class “outside the royal circle” and high rates of urbanization. In countries where monarchies had an absolutist control, such as Portugal, Spain and France, there was a greater tendency to grant trade monopolies thereby preventing broad-based economic and property rights reforms. The evidence presented by Acemoglu and colleagues strongly dismisses popular explanations for European divergence that are centered on the role of religion, geography and the type of heritage (Greek or Roman). Instead, it was the confluence of these mutually reinforcing forces that explain the European divergence rather than other popular explanations, such as religion, Roman or Greek heritage or a country’s geography.

### ***Islamic law and the enforcement environment***

Kuran emphasizes the binding, autonomous and rigid (inflexible) nature of Islamic law as it is based on religious texts. This apolitical analysis of pre-modern Middle Eastern legal system defies the actual realities. The public administration was regulated by imperial decrees called *kanun*, which was secular in nature. In commercial sphere, custom played an important role. This legal segmentation reflected political preferences. Arenas where political stake was high were governed by ruler’s law and as the religious class was incorporated into state bureaucracy, Islamic law became a handmaiden of the political elites. This is evident by the circumvention of Islamic inheritance law on land. As the land was a crucial source for political power, it was regulated by secular law rather than Islamic law.

Theoretically, Kuran’s emphasis on inheritance law as a source for discouraging the accumulation of wealth seems correct. However, in many parts of Muslim world, customary practices rather than inheritance law, governed the distribution of a deceased person’s property. Moreover, Islamic law itself provided some mechanisms to circumvent inheritance law in the form of family waqf and inter vivos gifts in order to transfer family wealth to a favourite child. Recent research based on archives also refutes Kuran’s thesis that Islamic law caused fragmentation of family wealth.<sup>16</sup> A doctoral study completed at

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<sup>16</sup> M Cosgel and BA Ergene, 'Intergenerational Wealth Accumulation and Dispersion in the Ottoman Empire: Observations from Eighteenth-Century Kastamonu' (2011) 15 *European Review of Economic History* 1.

Harvard in 2008 on family business in the Gulf States shows that various mechanisms were employed in order to ensure intergenerational succession of family business without fragmentation. These included traditional cultural norms that dictate respect for elders, employment of siblings in business, equality of treatment and participation of family members and employment of non-family professionals in running of the business. In most cases, the eldest son succeeded assuming a patriarchal role emphasizing kinship, mutual interdependence and family reputation.<sup>17</sup> The problem of dispersion of ownership caused by inheritance law was overcome by purchasing the share of exiting members or by consolidating one branch of family under a firm expressly created for this purpose.<sup>18</sup>

The waqf was the only permanent institution, which had the corporate features under Islamic law. As it was not mentioned in the Quran and was merely alluded to in the traditions of the Prophet, the institution itself developed over the period of time. Initially the waqf was used for the provision of public services. However, it became wide spread for the accumulation of family wealth in the later periods of Islamic history. A large number of waqfs were created all over the Muslim world in favour of family members with nominal income vested in favour of some charitable public cause. Historically the public and private functions of the waqf were intertwined. In fact this ambiguity in the nature of waqf made it an attractive legal tool for the protection of private property from predatory state authorities. The waqf originated and remained a religious and charitable institution despite the fact that it was used for multifarious functions including mundane objects. As against Islamic commercial partnerships, the waqf responded to social changes and was also used to provide financial services in the form of cash waqfs.

Kuran acknowledges the adaptability of the waqf and appreciates its historical functions. However, he points out that unlike the corporations, the waqf was economically inefficient because of its perpetuity, inflexibility, lack of self-governance and absence of separate legal personality (pp110-15). He considers that the waqf was suited to a pre industrialised society but lacked dynamism to fulfill the requirements of a modern society. The 'static perpetuity' of waqf restrained it from developing into a dynamic institution same as the Western corporations (pp160-1). Kuran's analysis of the waqf depicts it as a product of peculiar medieval circumstances. Unlike the inheritance laws, the bulk of the waqf law was drawn from the secondary sources of Islamic law. In case of cash waqfs, the law responded to the practice on public interest and pragmatic considerations. However, the waqf as an institution remained inherently inferior to both the trusts and corporations.

### ***Law, commercial practice and organisations***

With respect to commercial law and practice, there arises the question about sequencing: does commercial practice lead to legal changes? Commercial law is often retroactive rather than pro-active. Legal evolution follows commercial demands. If there were sufficient demand, it might have led to legal innovations or more efficient forms of

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<sup>17</sup> Jaidah, MJ, 'Explaining Multi-generation Family Business Success in the Gulf States' (Harvard University 2008) 231-34.

<sup>18</sup> Ibid, 239.

circumventions.

Kuran rejects the market based demand led explanation for the development of large scale business corporations in favour of his law matters thesis which focuses on the interplay of inheritance law and primitive contract/partnership law of Muslims. According to his thesis, the Middle East should have lacked permanent commercial organisations since the legal system failed to recognise them or was even unable to accommodate them. However, large scale organisations were formed in areas which required pooling of huge resources such as tax farming and export of food items. Interestingly, unlike the private sector, the public sector exhibited enormous development and transformation.

The history of business organizations in Europe reveals that the joint stock company was a creative response to the peculiar political and economic conditions of Europe. The competitive overseas trade required large resources for longer periods of time and a new form of business was needed to facilitate resource pooling. European governments wanted to generate revenues and expand political influence by issuing charters to merchants. Industrial Revolution promoted and facilitated the development of corporations in capital and labour intensive ventures. As mentioned before, the Ottoman Empire lost out on long distance trade. Economic opportunities that could have aided the formation of large scale organizations were simply absent. Moreover, it discouraged the formation of business organizations fearing their powers. The stagnant economy did not generate any need for permanent business organizations like modern corporations. Therefore, the economic lag of the Middle East coupled with the lack of political will may have been the main reason for the organizational underdevelopment in the Middle East. Shares were issued and a secondary market to deal with such shares had also developed to finance the state. Within a short span of time the Ottoman taxation system transformed from *timar* (fief-holding) to *iltizam* (tax-farming) and from *iltizam* to *milkalane* (life time tax farm holding) and *seham* (shares or bonds). Innovative techniques were developed by the active private sector to benefit from the lucrative profits offered by the state in return for providing public finance. Thus private savings were mobilised, intermediary financial services industry developed and new techniques formulated to raise capital.<sup>19</sup>

In Prof. Kuran's analysis, corporations stand out as one of the key elements behind the success of the West vis-à-vis the Middle East. It is asserted that since Middle Eastern partnerships failed to develop into corporations or their equivalents, it failed to develop both economically and politically. However, Kuran's analysis is based on certain assumptions about the history of business organisations in both the Middle East and Europe. Unlike Europe, where history of corporations is interlinked with merchant guilds, Kuran tries to trace an evolution of private partnerships in the Middle East. Hence the absence of juristic personality and the simplicity of contractual partnerships under Islamic law are shown to be detrimental to organisational evolution. In this analysis, Kuran relies upon the earlier work of Murat who compares the evolution of partnerships

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<sup>19</sup> M Çizakça, 'Evolution of Domestic Borrowing in the Ottoman Empire' in PL Cottrell (ed) *East Meets West: Banking, Commerce and Investment in the Ottoman Empire* Ashgate Publishing Limited 2008) 1-10.



in the Ottoman Empire and the West. Murat ignores Ottoman guilds in his comparative study, as they do not fall under the definition of partnerships.<sup>20</sup> However, this leads readers to believe that these were the partnerships in Europe, which developed into joint stocks and later into modern corporations. Thus the crucial link of guilds in the development of modern corporations is entirely ignored. Kuran touches upon the issue of Ottoman guilds in his book. He finds that the guilds in the Ottoman Empire were not independent of state and did not have internal governance as was the case in Europe. He also mentions two opposing views regarding whether such guilds enjoyed juristic personality. Here Kuran is more candid and accepts that the reason guilds could not gain more autonomy lies in ‘political conditions’ as the state kept guilds under its authority and denied them independent growth.<sup>21</sup> But Kuran fails to appreciate the co-evolution of guilds and partnerships under state patronage in Europe.

From the methodological perspective, Prof. Kuran’s primary focus is on the aspects of Islamic law that hindered evolution of private organisations in the Middle East. He acknowledges the lack of demand for corporations as one of the possible explanations for institutional underdevelopment in the Middle East, but justifies his approach by pointing out the reasons for giving ‘analytical priority’ to the impact of inheritance law on private business: (a) private organisations are the key determinant of state capabilities; (b) economic life, not public administration explains the Middle East’s failure; and (c) historians have devoted more attention to the role of the state than that of private organisations.<sup>22</sup> Regarding alternate explanations for the Middle Eastern underdevelopment such as geography, the state and scientific knowledge, Kuran argues that a bidirectional causal relationship exists between any two variables. This makes any starting point of inquiry ‘ultimately arbitrary’.<sup>23</sup> A better approach could have been a study based on the co-evolution of public and private institutions in the Middle East. As Avner Grief notes:

“Corporations reflect the intentional coordinated effort to create institutions as well as a means for doing so. They produced legitimate rules and altered self-enforcing beliefs in a central economic or political transaction by linking them to other economic and coercive – legal or otherwise – transactions. Incentives were often provided by both economic reputation and coercion” (Greif 389).

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<sup>20</sup> M Çizakça, *A Comparative Evolution of Business Partnerships: The Islamic World and Europe, with Specific Reference to the Ottoman Archives* (Brill 1996).

<sup>21</sup> T Kuran, *The Long Divergence: How Islamic Law Held Back the Middle East* (Princeton University Press 2011), 132-33.

<sup>22</sup> *Ibid*, 16-9.

<sup>23</sup> *Ibid*, 15.